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Nos. 83-737 and 83-738

In the Supreme Court of the United States

OCTOBER TERM, 1983

THE PEOPLE OF THE STATE OF CALIFORNIA and THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA, *Appellants*,

vs.

UNITED STATES OF AMERICA, AMERICAN TELEPHONE & TELEGRAPH COMPANY, ET AL., *Appellees*.

NEW YORK STATE DEPARTMENT OF PUBLIC SERVICE, *Appellant*,

vs.

UNITED STATES OF AMERICA, AMERICAN TELEPHONE & TELEGRAPH COMPANY, ET AL., *Appellees*.

On Appeal from the United States District Court for the District of Columbia

MEMORANDUM IN SUPPORT OF JURISDICTIONAL STATEMENTS

James H. Bailey
General Counsel
Eddie M. Pope*
Assistant General Counsel
Oklahoma Corporation Commission
Room 460, Jim Thorpe Building
Oklahoma City, Oklahoma 73105
Telephone (405) 521-2255
Attorneys for Appellees

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*Counsel of Record

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The Oklahoma Corporation Commission ("Oklahoma") is the regulatory agency with jurisdiction over rates and practices of telephone companies in Oklahoma. Oklahoma was a party below in *United States* v. *AT&T*, 552 F.Supp.

131 (D. D.C. 1982), *aff'd mem. sub. nom. Maryland* v. *United States*, ___ U.S. ___, 103 S.Ct. 1240, 75 L.Ed.2d 472 (1983). Pursuant to Rlue 10.4 of this Court, Oklahoma is an Appellee. Oklahoma supports the position of Appellants, People of the State of California ("California") and New York State Department of Public Service ("New York"). This Court should note probable jurisdiction in these cases and set them for plenary review.

Oklahoma adopts the Jurisdictional Statement of California for the description of the Opinions Below, Jurisdiction, Statutory Provisions and Statement of the Case.

THE QUESTIONS ARE SUBSTANTIAL

As the District Court recognized, the AT&T divestiture is the "largest corporate reorganization in history" affecting "millions of employees and shareholders, the nation's telephone subscribers, AT&T's competitors, the telecommunications industry . . . and the responsibilities of federal and state regulatory bodies," App. at 353.

The immensity of this case is illuminated by the fact that the questions regarding station handling costs and complex inside wiring are not major issues in the case below — but represent over three *billion* dollars nationwide just for complex inside wiring, untold billion dollars for station handling costs; for Oklahoma, the investment represents $25 million for complex inside wiring and approximately $41 million for station handling costs. In any other case, these would be substantial numbers.

It is not just the numbers that make this case substantial.

The claimed error in this case is fundamentally one of disagreement over accounting. The experience of state telephone regulators was, in key respects, disregarded by a federal district court judge. Due to the press of time and certification in this case, this Court is the only forum in which the error can be corrected. This Court should allow the states a chance to present their case.

This case affects every telephone subscriber in America. It is a uniquely national case.

Understanding this case requires an understanding of some aspects of telephone engineering and accounting. These are fields coated with jargon. Oklahoma will try to cut through the complexity and present a simple explanation.

In the past, when you called the phone company for totally new phone service, the company would send a service agent who would string a wire from the nearest telephone pole to your home. In technical terms, this is the "drop wire" to the "protector". The protector is frequently on the outside of the residence and protects the phone system from damage from lightning. Then the service agent would wire the inside of the house from the protector to the service jack. This is "simple inside wiring". The service agent would install the telephone and test it. This is "station handling".

There are differences with business systems. If a business has several incoming lines or several telephones tied together with an intercom, it has "key system apparatus" or "private branch exchanges" ("PBXs"). Wiring these telephones together is more difficult and requires more time

of the service agent than residential-type wiring. It is called "complex intrasystem wiring".

In the past, the costs of all these "station connections", both residential and business, was accounted for in Account 232 of the FCC's Uniform System of Accounts. They were "capitalized", that is, treated as long-term investments on which the telephone companies earned a rate of return. This long-term recovery of these costs was chosen so as to keep as low as possible the initial cost of hooking up to the system. This encouraged widespread installation of telephones for everyone, or "universal service."

This long-term recovery caused problems because the sum of these station connections continued to grow. In 1979, the Bell system installed approximately 36 million telephones and removed approximately 31 million telephones, *Amendment of Uniform System of Accounts*, 85 F.C.C.2d 818, 824 (1981). All of the costs of these changes, including the labor charges, were booked to Account 232.

The FCC recognized this enormous capital outlay was a burden to the system. In 1981, it ordered all future inside wiring to be "expensed", that is, treated as an operating expense which allows for a far more rapid recovery of the costs. (The drop wire and protector continued to be capitalized.) The FCC authorized the accumulated inside station connection and inside wiring investment to be recovered over a ten-year amortization period.

In 1980, the FCC moved to deregulate "customer premises equipment" (CPE), which includes telephones, PBXs and key units. In the first order the Commission excluded inside wiring from the definition of CPE, *Amendment of*

Section 64.702 of The Commission's Rules and Regulations (Second Computer Inquiry) Docket No. 20828, 77 F.C.C.2d 384, 447, 35 P.U.R.4th 143, 205 n.57 (1980). In a subsequent order, the FCC stated that the issue of inside wiring "was not addressed" in earlier proceedings, and was specifically reserved for a later proceeding, 84 F.C.C.2d 50, 69, 39 P.U.R.4th 319, 341 (1980).

On January 8, 1982, the parties in the AT&T antitrust case filed a stipulated "Modification of Final Judgment". On August 11, 1982, Judge Greene filed his opinion in that case (App. 1-172), and the companion Modification of Final Judgment was filed August 24, 1982 (App. 173-190). The Modification of Final Judgment assigned to AT&T "all facilities, personnel and books of account . . . relating to . . . the provision of customer premises equipment to the public." (MFJ, §§I(A)(2), I(A)(4); App. at 174-175.) "Customer premises equipment" was defined as "equipment employed on the premises of a person . . . to originate, route or terminate telecommunications," not including "equipment used to multiplex, maintain or terminate access lines." (MFJ, §IV(E); App. at 177.)

On December 16, 1982, AT&T filed a Proposed Plan of Reorganization. That plan assigned all of the customer premises equipment to AT&T, but all of the embedded cost of installing that equipment (Account 232) to the proposed new regional Bell Operating Companies (BOCs). Several state commissions and the National Association of Regulatory Utility Commissioners protested the assignment of the inside wiring and station handling costs to the BOCs.

On February 28, 1983, this Court affirmed the Modified Final Judgment, *Maryland* v. *United States*, ___ U.S. ___,

103 S.Ct. 1240, 75 L.Ed.2d 472 (1983). The treatment of the issues relating to station connections were still being litigated. On March 14, 1983, AT&T filed its "Response to Objections to its Proposed Plan of Reorganization". It claimed there was "no way" to determine station handling costs (p. 154) and claimed "no distinction" could be made for complex inside wiring (pp. 154-155). Even AT&T noted, however, that New York was already charging separate charges for inside wire (p. 163, n.**).

State commissions protested that the various elements of Account 232 *could be* and *had been* segregated (Comments, N.Y. Dept. Pub. Serv. at 11; Further Comments, Calif. Pub. Util. Com'n at 24; Reply Comments, CPUC, at 26).

The District Court conditionally approved the Plan of Reorganization on July 8, 1983 (App. 195-330). There was *no* mention of the complex intrasystem wiring and station handling claims. On July 28, 1983, the District Court dealt with an AT&T Motion for Partial Reconsideration. It dismissed Account 232 claims along with "patent licensing" claims in a footnote (App. at 339, n.18).

The modified Plan of Reorganization was approved by the District Court on August 5, 1983. In the memorandum approving the Plan, the court described AT&T ownership of inside wiring as creating a "bottle-neck". The court was persuaded by AT&T that "there is no practical way to separate" the various costs (App. at 344). The District Court did acknowledge that "a theoretical case could be made" that some portion of Account 232 should follow the embedded customer's premises equipment.

The case is more than theoretical. The states had demonstrated that AT&T's costs *could* be separated in a reasonable manner. The District Court should have deferred to the experience of the state regulatory agencies, and conditioned approval of the Plan on the appropriate allocation of these costs to AT&T.

District courts should have a "scrupulous regard" for state public service commissions, *Alabama Public Service Com'n* v. *Southern Railway Co.*, 341 U.S. 341, 349 (1951). The ratemaking process is "essentially empiric. The stuff of the process is fluid and changing . . ." *Board of Trade* v. *United States*, 314 U.S. 534, 546 (1942). It is not an area well suited for court determination. The District Court should have granted great deference to the experience of state regulators. If state regulators say an account can be meaningfully divided, the courts should recognize that it probably can be divided. This Court has recognized that such disputes are:

> for the regulatory commission and not for the courts. We repeat that for a court to upset an accounting order it must be 'so entirely at odds with fundamental principles of correct accounting' . . . as to be the expression of a whim rather than an exercise of judgment. — *United States* v. *New York Telephone*, 326 U.S. 638, 655 (1946)

The state regulatory commissions have established reasonable accounting distinctions for separation of Account 232. The Federal Communications Commission has detariffed intrasystem wiring installed in the future, *In the Matter of Modifications to the Uniform System of Accounts for Class A and Class B Telephone Companies*, CC Docket No.

82-681, Order November 2, 1983. The regulatory judgment is that the purchaser of the customer premises equipment should pay for the costs of installing that equipment. The District Court erred in placing the equipment with AT&T, and the installation costs with the Bell Operating Companies.

The District Court contradicted its own prior order. The District Court should have recognized that station handling and complex intrasystem wiring were part of the "books of account . . . relating to . . . the provision of customer premises equipment to the public" (MFJ, §§I(A)(2), I(A)(4); App. at 174-175). The District Court should have corrected AT&T when it assigned some accounts of the wiring used "to originate, route and terminate telecommunications" (MFJ, §IV(E); App. at 177) to the Bell Operating Companies.

CONCLUSION

The District Court contradicted the judgment of experienced state regulatory commissions. The District Court contradicted equitable principles that the person receiving the benefit (*i.e.*, CPE) should pay the costs associated with that benefit. If this Court does not correct the contradictions, every telephone ratepayer in America will be required to pay their local Bell companies for the accrued cost of installing equipment that AT&T now owns. This Court is now the only chance to rectify that error. This Court should note probable jurisdiction in the appeals filed by California and New York.

Respectfully submitted,

JAMES H. BAILEY
General Counsel

EDDIE M. POPE*
Assistant General Counsel
Oklahoma Corporation Commission
Room 460, Jim Thorpe Building
Oklahoma City, Oklahoma 73105
Telephone (405) 521-2255

Attorneys for Appellees

*Counsel of Record